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## The Effect of Service Quality and Marketing Mix Strategy towards Local Sustainable Economic Growth

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**Abstract:**

*The purpose of the study is to investigate the effect of service quality and marketing mix strategy towards local sustainable economic growth.*

*This type of research is explanatory because the purpose is to explain the causal relationship between variables by testing the hypothesis. Target population in this study are all customers or service users who use the product of MSME, and the total number of the sample used is 200. The analysis tool used is Structural Equation Modeling (SEM).*

*The quality of service effect on marketing mix strategy means that the application of quality of service, according to customer needs, is able to create satisfaction. In other words, the better the quality of service provided to customers the higher the increase in satisfaction. The quality of service directly creates local sustainable economic growth, that means improved quality of service provided by the company to customer needs, thereby increasing local economic growth. The quality of service is influencing the local economic growth through the marketing mix strategy.*

*Marketing mix strategy has a significant positive effect on local sustainable economics, indicating that the higher the marketing mix strategy, local economic growth will be higher as well.*

*The mediation effect and the concept of marketing mix strategy on the effect of service quality toward local economic growth as well as the location of the study (no previous research for this relationship) can be considered as the main originalities of this research.*

**Keywords:** *Service Quality, Marketing Mix Strategy, Local Sustainable Economics.*

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## 1. Introduction

Research into small and medium- sized enterprises (MSMEs) has grown during the last decade due to the fundamental contribution of this business sector to the overall performance of the economy. Between 90.0 and 99.0 per cent of firms worldwide are MSMEs, of which the majorities are very small or even microenterprise firms. Emerging business practices, such as flexible production, downsizing, outsourcing and franchising, support the trend towards MSMEs, and as a result they playing an increasingly significant role in the stability, job creation and economic development of a nation (Gutierrez *et al.*, 2015; Akopova *et al.*, 2017; Bondarenko *et al.*, 2017; Robertie, 2016; Menshchikova and Sayapin, 2016; Medvedeva *et al.*, 2016).

Small bussiness is a term in the development of the Economy of Indonesia that plays an important role to preserve the national economic growth in the post-economic crisis period. In addition is a business sector that gives a great contribution to the development creating great job chances for domestic labor increase decreasing the unemployment rate. The economic crisis resulted in decreasing the economic growth in the monetary and financial sectors, especially in the real economic structure. Before the crisis, the government put more priority on the upstream but ignored the downstream industries. There was a statement that, if the upstream industry is developed then the downstream industry will follow.

The fact is that the developed large industries remain vulnerable to the external shock because they do not have any backward and forward linkages in providing inputs. It was late-anticipated by the government in introducing MSMEs as a program to build the downstream industry and pro-big business development. As a result, the downstream industry experienced lameness during the economic crisis. It is a different case when the government implemented the MSMEs program as a solution in overcoming the problems faced by downstream industries. MSMEs become a solution in overcoming the crisis, since MSMEs rely more on programs conducted as the excellence-based programs (Bauchet and Morduch, 2013).

MSMEs can prove that the downstream industry sector can be the foundation for the national economy compared to the upstream industry that tends to crash (Rupeika-Apoga and Solovjova, 2016). It is proved by the increasing number of MSMEs, both in small and medium scales, every year. In the developing countries, MSMEs are a major economic activity that gives revenue contribution and creates great labor absorption rate. MSMEs in Indonesia are an economic activity that gives a great contribution to the Gross Domestic Income (GDI) and absorbs labor from rural communities by creating many employment chances in the downstream industry sector that reinforced the stability of the national economy. Its role is expected to create welfare for the Indonesian people (Kemenperin, 2017).

MSMEs occupy a strategic position in the economy of Aceh. MSMEs play a role in creating jobs and empowering the people's economy. The number of MSMEs in

Aceh reaches 55.783 units, consisting of micro businesses 39.571 units (71%), small businesses 13.728 units (25%), and medium enterprises 2.484 units (4%) (Dinas Perindagkop and UKM Aceh, 2016). It is estimated that currently, MSMEs in Aceh have absorbed about 275 thousand workers. This MSMEs move mainly on the sectors of trade, services, agriculture, industry, and fisheries and marine.

The role of determining MSMEs for the economy of Aceh is in line with the contribution of MSMEs to the national economy. Data from the State Ministry of Cooperatives and MSMEs in 2015 shows a significant contribution of MSMEs nationally. First, the MSME industry in the economic sector reaches 99.9% of the total business units. Second, the ability of MSMEs in absorbing labor reached 97.04% of the total workforce. Third, MSMEs contributes 55.56% in the formation of gross domestic product (GDP). Given the important presence of MSMEs, the Government of Aceh should seriously support the pace of this economic undertaking. Government policies to develop and strengthen MSMEs in economic activities need to be formulated and implemented with precision and care. The policy should lead to the creation of a conducive business climate, business development support, quality improvement of human resources, and institutional strengthening of MSMEs.

The government is asked to improve the MSMEs empowerment program because this sector supports the Indonesian economy especially in the midst of the current crisis. MSME's role can no longer be ignored because almost 90 percent of the national economic sector is supported by MSMEs and almost all the lower middle class is helped by this sector. MSMEs in Indonesia can survive in times of economic crisis. The majority of MSMEs rely more on non-bank funds in the business financing aspect. In general, MSMEs conduct strict product socialization, in the sense that they only produce certain goods and services. MSME in Indonesia has an important role as a supporter of the economy because the main driver of the Indonesian economy so far is the MSMEs sector.

Some of the main functions of MSMEs in moving the Indonesian economy are; their role as a provider of employment for millions of people who are not accommodated in the formal sector; MSME sector also contributes to the formation of Gross Domestic Product; MSME sector as a source of foreign exchange earners through the export of various types of products produced by this sector.

MSME is required to recognize, understand, and fulfill the need of their customers better than their competitors do. If the need and the demand of their customers has been fulfilled, it means that a basic expectation of their customers have been fulfilled. If the expectation is compared to performance that reflected from the goods or services, then the fulfillment of satisfaction or dissatisfaction may be determined. Marketing mix strategy has been a part of goals for most companies. Other than gaining profit or big advantage, it also aimed as an effort to survive in the tight competition. Meanwhile, service quality, especially for the service companies, is an

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important thing to give more satisfaction to customers, which finally become a value added to the company itself.

The company must recognize and observe how to create and improve the quality of goods and services that offered. A service quality that created and has been improved cannot be measured from the company's perspective, but it should be derived from customers' perception (Kotler, 2001). Application of quality is a main part of company's strategy to gain a continuous superiority, either as a market leader or as a strategy to keep the growth and survive. Quality is an effort to meet or even to exceed the customer's expectation. It includes the products, manpower, processes or environment. Tjiptono (2005) revealed that a good quality of service will encourage the customers to have a bond, a strong relationship with the company, this kind of bond enable the company to more understand their customer need and expectation.

Therefore, the company may improve the marketing mix strategy by maximizing the customer's good experience and minimizing their bad experience. Through the marketing mix strategy, it is expected that the loyalty to be created where the customer will re-use or re-purchase the products and cannot be easily influenced by other product along with providing a free promotion to the company by recommend the company's products to other customers. Loyalty building is the most effective way to reach a constant profit growth. The best customer is the most loyal customer. Therefore, a company must be able to identify, maintain, and strengthen the loyalty.

The expose of the service quality in this research (servqual) even though many researches have been conducted on the same issue is because a MSME is required to have an effective service quality to satisfy its customers and to make them loyal to the product that offered. Service quality that referred in this study is service quality that is provided to the customers. A service that promoted a personal assistance will provide the MSME customers with a human and respected service. A personal assistance strategy that applied should be in line with capability of the personals that carry out the service, which means, the company must have a human resource that is capable and able to communicate with customers, to convey information as well as to receive the complaints from the customers. Besides, the service quality is also related with speed, product innovative movement, and speed in accessing information accurately and quick responses.

Customers choose a product based on utility value and value of favoritism or fun (hedonic) (Batradan, 1991). The value of fun and happiness is a result of feeling, experience, fantasy or affective (Hirschman and Holbrook, 1982). While, a value of utility or functional is more affected by customer cognitive aspect to act objectively (Strahilevitzdan, 1998). As a result of trust and effect of the product that will encourage the customers to loyal with the product that reflected in the repurchasing (purchase loyalty) and attitudinal loyalty to stay with the product (Aaker, 1991).

A product that can build a local economic growth through the two values above (utilitarian dan hedonic) encouraged a customer's trust. Based on the background discussed above, the aim of this study is to investigate the effect of service quality, and marketing mix strategy towards local sustainable economic (study in MSME in Aceh). The originality of this study is associated with the mediation effect, marketing mix strategy on the effect of service quality toward local economic growth and the location of the study.

## **2. Literature review**

The quality concept is depending on the perspective that is used to determine characteristics and spesification. Basically there are quality orientations that should be consistent one to another such as : (1) customer perception, (2) product/service (3) processes. As for the material form, this orientation can be easily distinguished even if the product is only a process. Quality consistency of a service for the three orientations may contribute to the success of a company if perceived from a marketing mix strategy, employee's satisfaction and organization profitability.

In a more competitive global competition situation, product quality, either in goods or services, is a critical issue for every company. The ability of the company in providing a qualified product, is a weapon to win the competition, because by providing customer with a qualified product, marketing mix strategy may be achieved. But the word of quality may be confusing if it had to be perceived similar to every person. Therefore, a company must determine a proper definition and accurate understanding about the quality.

The professional businessman and quality consultant have agreed that the word 'quality' has a universal meaning. In 1978 quality definition is formalized by The American National Standards Institute (ANSI) and The American Society for Quality (ASQ) as totality of features and characteristics in a good or service embedded in its capability to satisfy the expected demand. In the 1980s, many companies used a more simple term but still have a full power, such as quality is to meet or to exceed the customer expectation. There are five model dimensions of the Servqual (service quality) that developed by Parasuraman, Zeithaml and Berry, as quoted by Zeithaml and Bitner (2000) as follows:

1. **Tangible** is the materialized/physical evidence, reliability, responsiveness, assurance and empathy.
2. **Reliability**, is the company's ability to provide services to the promise of accurate and reliable.
3. **Responsiveness**, is the ability and the willingness of the company to help and provide fast service (responsiveness) to the customer.
4. **Assurance**, is knowledge, behavior, and the ability of the firm's employees to foster the confidence of customers to the company and the ability to create a sense of security for customers.

5. **Empathy**, is providing a genuine concern, individual or personal to its customers and strives to understand the needs and desires of customers.

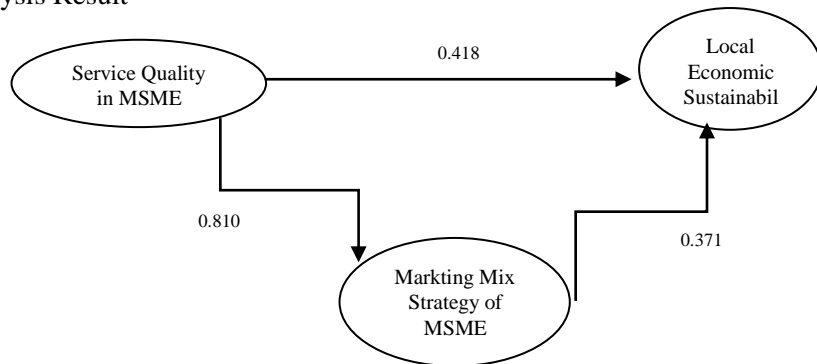
Marketing mix strategy is a central concept in business discourse. Customer is a main focus in a discussion on satisfaction and service quality. Therefore, customer play an important role to measure the satisfaction on the certain product or service that provided by the company. The word satisfaction is derived from the latin word, *satis* which means quite good or adequate, and *facio* which means to do something. Rambat (2001) quotes Kotler (1997) that defines satisfaction as the level of feeling when someone described a comparison result on the product performance and or service that received and expected.

Meanwhile, according to Webster's 1928 Dictionary, as quoted by Lupiyoadi (2001), customer is someone who came several times to purchase a product or service. So, a customer is someone who come continuously to a same place to satisfy his demand on a product (good) or to receive a service and pay for the product (good) or service. A benefit gained from a marketing mix strategy is extremely big, but, recently, the marketing mix strategy is no longer a final purpose in a business process of a company. Many companies depend the marketing mix strategy on future successes and they are dissappointed at the end when they realized that their product is far behind from their competitor's product.

The value of a small business sector is recognized in economies world-wide, irrespective of the economy's developmental stage. The contribution towards growth, job creation and social progress is valued highly and small business is regarded as an essential element in a successful formula for achieving economic growth. The World Bank (2007), however, estimated that the MSME contribution to employment generation was 66.9% in India. China's MSME sector contributed highest 78% to its total employment with the lowest rate in South Africa (39.6%).

The contribution of MSMEs in India to economic development is highly remarkable comparing to any other sector of the economy. Their role towards investment, employment generation, export, GDP, industrial production etc., is highly significant. Figure 1 clearly exposes their significance towards economic development. It is clearly indicating that MSMEs registered a very high growth rate. This is mainly due to its various advantages comparing to other sectors, while Indian economy which is more close to MSMEs environment, likes cheap local resources, local talents, high demand etc. Moreover the socio-economic policies adopted by India since the industries development and regulation Act in 1951 have laid stress more on MSMEs sectors as a vehicle to develop the Indian economy. Second five-year plan also gave more emphasis on industrial development and adopt various policies for proper development of this sector. Investment and production are closely linked. More investment indicate more production or more production require more investment.

Figure 1. Analysis Result



### 3. Research methodology

This type of research is explanatory because the purpose is to explain the causal relationship between variables by testing the hypothesis. A market survey to collect data that is needed in this research has been made by distributing questionnaires to be filled out by respondents in accordance with the characteristics of the population. According to Singarimbun (1999), the population is divided into two, namely population sampling and target population. Target population in this study is all customers or service users who use the product of MSMEs. The population of samples taken in accordance with the provisions set for the benefit of SEM analysis tools. According to Hair *et al.* (2010) in determining the size of the sample for SEM there are few guidelines that must be fulfilled, one of these, is depending on the sample size parameter of the estimation method in use. When using a parameter estimation method as the Maximum Likelihood Method (ML), the recommended sample size is between 100-200.

Based on the determination of the sample according to Singarimbun (1999), Augusty (2005) and Hair *et al.* (2010) the sampling indicators that form the basis for sampling in which there are 20 indicators that are used with a ratio of 5 observations, the number of samples used is  $5 \times 20$  parameter = 100 samples per customer of MSME. Therefore, 100 samples for the city of Aceh and 100 samples for the town of Lhoksumauwe. This sample has met the required number of parameters to be able to use the technique of Structural Equation Modeling (SEM), with the sample size to be between 200-300. The sampling technique used was purposive sampling, the sampling determination techniques tailored to the needs of the research. The implementation of sampling in this study conducted by accidental sampling which is doing research when researchers met with the respondent.

The analysis used is Structural Equation Modeling (SEM). SEM is a multivariate statistical technique which allows the testing of a series of causal relationships between variables simultaneously and in units so as to provide statistical efficiency.

Each exogenous and endogenous variable can be either latent or unobservable can be measured directly in the research process (Hair *et al.*, 2010).

#### 4. Results

The model is said to be good if the development of the hypothetical model theoretically has supported by empirical data. Detailed SEM analysis results are shown in the following Table 1. From the evaluation of the eight criteria the model shows a goodness of fit indices. Only one has not met the criteria that is TLI variable which is approaching the critical value to be accepted (marginally accepted).

**Table 1. Critics Evaluation Goodness of Fit SEM**

Goodness of fit index	Cut-off Value	Result Model*	Explanation
$\chi^2$ – Chi-square	Expected small	57.370 <(0.05: 42 = 386.125)	Marginal
Probability	$\geq 0.05$	0.057	Good
CMIN/DF	$\leq 2.00$	1.366	Good
RMSEA	$\leq 0.08$	0.045	Good
GFI	$\geq 0.90$	0.947	Good
AGFI	$\geq 0.90$	0.901	Good
TLI	$\geq 0.95$	0.882	Marginal
CFI	$\geq 0.95$	0.925	Good

Based on the empirical model proposed in this study it can be conducted that the hypothesis testing used is accepted, p values are less than 0.05% (Table 2).

**Table 2. Hypothesis Examination of SEM Analysis**

HIP	Independent Variable	Dependent Variable	Direct Effect			
			Standardize	CR	p-value	Explanation
H1	Service Quality	Marketing mix strategy	0.810	7.658	0.000	Significant
H2	Service Quality	Economic Sustainability	0.418	3.722	0.000	Significant
H3	Marketing mix strategy	Local Economic Sustainability	0.371	3.233	0.001	Significant
Indirect Effect						
Independent Variable	Dependent Variable	Intervening Variable	Standar Dize	Explanation		
Service Quality	Marketing mix strategy	Local Economic Sustainability	0.301	Significant		



The result shows that there is a significantly effect of service quality of MSMEs in Aceh to local economic sustainability. The higher the value of service quality the higher the value of local economic sustainability. It also shows that the marketing mix strategy, as the mediation variable in the relationship between service quality toward local economic sustainability is significant.

## **5. Discussion**

This result shows that service quality in the MSME sector, has a positive relation and its effect is significant to marketing mix strategy. The cause is service quality provided by the MSME for its customer has brought a significant satisfaction for the customer. From all dimensions of service quality that is consisted by responsiveness, (a quick response), tangibility (physical appearance), empathy (personal and sincere attention), reliability (reliability of service, on time, accurate and carefulness) and assurance (assurance/capability assurance from the company/MSME) the result is significant. The entire dimension is significantly fulfilling the expectations, achievement, compatibility and satisfaction demanded by the customer. Service quality perception is defined as a customer's perception or impression to service quality provided by the MSME.

This result also shows that the customer perceived the service quality that provided by the company has met with what he has expected. This means that what customer expected from the service quality is matched with what he has experienced. It means that MSME has provided service quality to customer that is in line with what he has expected, so the service quality as mentioned, has created a marketing mix strategy. So, in evaluating service quality provided by the company or the organization, it should meet with the customer's expectation in order to create a satisfaction. Therefore, service quality that meets with customer's expectation shall create a satisfaction.

There is a positive relation and significant effect between marketing mix strategy and local economic growth in the MSME in Aceh. It indicates that the higher the level of satisfaction that customer's perceived, the higher the level of local economic growth created. On the contrary, the lower the satisfaction level that perceived by the customer, the lower the level of local economic growth to the MSME. The fulfillment of expectation, compatibility, service achievement, shall create a satisfaction to customer that shall create a local economic growth. Therefore, a marketing mix strategy is very determinant to local economic growth that reflected by attitude to consume the products of MSME and recommend positive thoughts about MSME to other persons/parties.

This result supports several theories and several previous results conducted by Ostrowski *et al.* (1993), Kandampully and Suhartanto (2000), Bowen and Chen (2001), and Caruana (2002). They all stated that marketing mix strategy has a significant effect to local economic growth. The significance of the marketing mix

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strategy effect toward local economic growth in MSME sector has supported by the research done by Utari (2004) and Abadi (2006). This result showed a significant relation to local economic growth to marketing mix strategy in Aceh. It means that all service quality indicators shall be significant to local economic growth if they previously experienced a satisfaction. Therefore, the marketing mix strategy is very determinant to local economic growth. This result is supported by several theories and several previous researches such as Caruana (2002), Parasuraman (1998) and Cronin *et al.* (1992). They said that if marketing mix strategy is tending to be a mediation of relation on service quality toward local economic growth, local economic growth is a success key, not only in a short term, but also a continuous competitive reliable strategy. Local economic growth has a strategic value for the MSMEs as well as other brands, and cannot be separated due to existence of a strong bond that tied up.

The activities of MSMEs in Aceh cover various economic sectors/subsectors with diverse products (commodities). To improve the effectiveness of MSMEs and their contribution to the regional economy, it is necessary to develop the superior products of MSME. The MSME's flagship products can be defined using criteria such as the effect of the product on employment absorption, the number of business units, access to raw materials, the range of product marketing, the contribution of products to the local economy, and other related aspects.

Provincial government and district/municipality governments through SKPA/SKPK related to the development of MSMEs need to cooperate with banks, associations of MSMEs, Kadin and academia to identify and determine the superior products of MSMEs in each sector/sub-sector of the economy in their respective regions. The KPA/SKPK involved here is not only the direct institution of developing MSMEs (eg., cooperative and MSME office), but also other agencies related to the sector/subsector where MSME has many activities (such as the industry and trade, agriculture and food crops, forestry, plantation, animal and animal health, marine and fisheries, and culture and tourism).

In order to be more objective and have a strong base, the determination of superior products of MSMEs can refer to the results of studies from credible institutions (Bank Indonesia, universities, etc.). The pre-eminent products of MSMEs that have been determined at the provincial and district/municipal levels need to be given legal weight so that it can become an official reference in the development of MSMEs. With this legal weight, the related SKPA/SKPK can run or support programs/activities of superior product development MSMEs more focused and comprehensive.

The development of superior products of MSMEs in Aceh needs to be supported by a reliable database system. Databases that collect data on MSME's flagship products, employment, investment value, and marketing research are essential for business activities and investment plans. This database should be easily accessible by

business actors of MSMEs, SKPA/SKPK and other interested parties. This database should also integrate related activities to facilitate the coordination and cooperation of such agencies. To facilitate the development of MSME's flagship product, a kind of MSME Development Forum is needed, involving stakeholders such as related SKPA/SKPK, MSME associations, banking, Kadin, and academia. This forum can be a forum for communication, coordination and collaboration between stakeholders, so that the development of MSME's flagship products can be done in a synergistic and effective manner.

Banks need to improve access to financing of MSMEs superior products through socialization of credit financing schemes, expansion of service networks, enhancement of cooperation with various parties (universities, etc.) for MSME development and development of credit distribution schemes. With regard to the development of credit schemes, flexibility in repayment of credit takes into account the commodity characteristics of various sectors. For agricultural commodities, for example, the production cycle time difference can be considered in the timing of credit repayment.

The development of MSME's flagship product also greatly requires expanding the reach of marketing. Infrastructure development efforts in production centers, especially in remote areas, leading to marketing sites, will help expand the reach of this marketing. In addition to the development of terrestrial infrastructure, enhancement of functions and services of seaports is essential, especially to increase exports of superior products.

It is also important the training and the mentoring program for MSME business actors and the institutional strengthening of MSME. Training and mentoring programs are directed to improve product quality and packaging, foster entrepreneurial spirit, and develop production technology and business management. Institutions of MSMEs (cooperatives, associations, etc.) can be strengthened, for example by enhancing the capacity of institutional management and expanding cooperation among business actors. The efforts to develop MSMEs in Aceh need to be done in a planned and integrated manner. Promoting MSME means helping to mobilize people's economy. Promoting MSME is thus a concrete step to tackle poverty and unemployment, which in turn contribute to improving people's welfare and regional economic growth.

## **6. Conclusions and recommendation**

Based on the results of research and discussion on the influence of service quality, marketing mix strategy and local economic growth can be concluded the following:

- (1) Quality of service effect on marketing mix strategy, this means the application of quality of service according to customer needs will be able to

- create satisfaction. In other words, the better the quality of service provided to customers the greater the satisfaction;
- (2) The quality of service directly creates local sustainable growth. That means that improved quality of service provided by the company increases local economic growth, but the quality of service to influence local economic growth through marketing mix strategy will improve the marketing mix strategy so that will have an impact on the formation of local sustainable economic growth ;
  - (3) Marketing mix strategy has a significant positive effect on local sustainable economic growth, indicating that the higher the marketing mix strategy the higher the local economic growth.

Based on the conclusion of this research, some suggestions are as follows:

- (1) Service quality provided by MSMEs should be improved in order to increase customers satisfaction and loyalty especially for MSME customers in Aceh;
- (2) The improvement of the satisfaction and the local economic growth may be implemented through a service quality improvement efforts. A company that is aware of its weak point and respond it with an immediate improvement is a company has a better prospect compared to a company that is irresponsive in making improvement. It means that service quality is very necessary effort in order to improve marketing mix strategy ;
- (3) To maintain and to improve the local economic growth through a service quality improvement, MSMEs management should observe the special service process that has a direct link with customers, such as a convenience in administrative service, connection improvement, addition movement, and the most important to increase customer trust through programs offered by MSMEs.

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